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IN THE

Supreme Court of the United States

ILLINOIS TOOL WORKS INC. AND TRIDENT, INC.,
Petitioners,

v.

INDEPENDENT INK, INC.,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

BRIEF FOR VERIZON COMMUNICATIONS AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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BRIEF FOR VERIZON COMMUNICATIONS AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

INTEREST OF *AMICUS CURIAE*

Amicus Verizon Communications is a major provider of wireless and land-line telecommunications and related goods and services.[1] Rapid change—in technology, in product definitions, in the state of competition—pervades its business. Verizon has been a frequent litigant in antitrust cases, including in this Court. *See, e.g., Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004); *Nynex Corp v. Discon, Inc.*, 525 U.S. 128 (1998).

[1] This brief was prepared in full by Verizon and its counsel. No other person made a monetary contribution toward its preparation or submission. By letters filed with the Clerk, petitioners and respondent have consented to this filing.

Verizon has a strong interest in the development of sound antitrust principles, including those defining "tying" law. To prevent the perverse use of antitrust law to impede efficient practices and legitimate competition, such principles should embody meaningful threshold requirements for antitrust intervention in a manner that provides workable guidance to the bench and bar. Sound antitrust principles should minimize both case-specific costs, such as erroneous condemnation of legitimate business practices and the costs of litigation, and, at least as important, should minimize the systemic costs inflicted by rules that either overreach substantively or are simply too difficult to apply reliably—costs that include the chilling effect on innovation, investment, and legitimate competition caused by the prospect of massive litigation expenses, unpredictable results, and treble-damages liability inherent in antitrust cases. Verizon here sets forth a general antitrust policy analysis showing the need, at a minimum, for a strict requirement of clear affirmative proof of market power as a condition of any tying claim.

INTRODUCTION AND SUMMARY OF ARGUMENT

This Court has held that a tying claim generally requires proof of market power over the tying product, as well as forcing of the purchase of a second separate product (the tied product), plus certain effects on the tied-product market. *Jefferson Parish Hospital Dist. No. 2 v. Hyde*, 466 U.S. 2, 12-16 (1984); *see Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 462, 464 (1992). The specific question presented in this case is whether the defendant's ownership of a patent on the tying product can properly give rise to a presumption of market power in the tying-product market. Petitioners, as well as others, persuasively show that it cannot, because any such intellectual property right is not even a close proxy for the required market power—an *economic* concept, present only if there are insufficient actual or potential substitutes in the eyes of buyers that the defendant can

profitably sustain a price significantly above competitive levels. *See Eastman Kodak*, 504 U.S. at 464 ("'the ability of a single seller to raise price and restrict output'"); *NCAA v. Board of Regents of Univ. of Oklahoma*, 468 U.S. 85, 109 n.38 (1984); *Jefferson Parish*, 466 U.S. at 27 n.46; R. Posner, *Antitrust Law* 195-96 (2d ed. 2001).

In this brief, we underscore that conclusion—and the inappropriateness of allowing intellectual property to serve even as a burden-shifting substitute for market power—by reiterating just how important is a strict requirement of market power to any sound doctrine for condemning tying under the antitrust laws. As an initial matter, conduct typically challenged as tying is substantively unilateral in nature: it involves no contractual commitments about whether the buyer will deal with rival sellers in future purchases, but merely the defendant's decision what to sell (two items together), which is comparable to the defendant's decision what to charge. The effect on rivals is like that of any simple sale: a de facto displacement of some of the buyer's interest in buying from someone else. Tying is therefore subject to the especially strong demands of antitrust law, when applied to unilateral decisions about how to compete, for careful justification and formulation of any ground of judicial intervention, taking full account of the possible benefits of the conduct, the difficulty of identifying when such conduct works antitrust harm, and the dangers that the systemic effect of a particular rule of illegality will (because of substantive overreach or unpredictability or difficulty of application) be to chill desirable competitive conduct.

Tying—selling two items only together, not separately—is ubiquitous in the economy. Critically, it is commonplace in competitive markets. That fact confirms that tying widely, and presumptively, serves efficiency interests, and it undermines any notion that tying should be viewed with suspicion. The benefits of tying—for example, in consumer convenience

and in production and packaging and transaction cost savings—are well recognized. An intrusive tying rule will therefore cause market harm. Yet concrete identification of such benefits is often difficult or impossible, so a rule that demanded proof of such benefits would erroneously condemn many beneficial ties.

The circumstances in which tying can be reliably judged to cause market harm are narrow and hard to identify in practice. The analysis of *Jefferson Parish*, and its elaboration in then-Judge Breyer's opinion in *Grappone, Inc. v. Subaru of New England, Inc.*, 858 F.2d 792 (1st Cir. 1988), indicate that the circumstances are a mere subset of cases in which the defendant has not only market power over the tying product but a likelihood of obtaining market power over the tied product. Recent economic literature about tying, which assumes away efficiencies (among its other acknowledged limitations), furnishes no basis for any more interventionist standard.

The other elements of tying doctrine themselves carry a high likelihood of erroneous determination and costly litigation—and hence add to the reasons a firm would have to shy away from conduct that might be accused of tying, even when it is efficiency enhancing and unlikely to work any market harm. It is expensive to litigate, and hard to predict the answer to, the question whether a sale involves separate products. The difficulties, and the risk of erroneous condemnation of beneficial ties, are especially great where technological change is substantial. Similar difficulties infect the element of "forcing" the purchase of the tied product, at least when the inquiry extends to the pricing terms of the package offered by the defendant. Finally, consideration of justifications for a tie poses its own dilemma: if excluded from the judicial inquiry, tying law is substantively too intrusive, condemning much beneficial conduct; if included in the judicial inquiry to avoid such overreach, the complexity and difficulty of litigation are increased.

In these circumstances, screening devices are essential to reduce the range of error and deterred competition. At a minimum, a strict requirement of affirmatively proven market power over the tying product is needed to serve that function; a second important screen is proof of a dangerous probability of market power in the tied-product market. A critical part of such screens is the assignment of a strict burden of proof to the plaintiff, which reduces the risks and costs of antitrust litigation that otherwise can be a powerful force for deterring competition. The importance of the market power screens makes it all the more damaging to allow any displacement by a poor substitute like the presence of an intellectual property right.

ARGUMENT

BASIC ANTITRUST POLICY REQUIRES AFFIRMATIVE PROOF OF MARKET POWER AS ONE ESSENTIAL CONDITION OF A TYING CLAIM

Other briefs filed in this case demonstrate the core reason for reversal of the Federal Circuit's judgment. The presence of a patent or other intellectual property right covering a particular product is so poor a proxy for any market power in the sale of that product—so badly corresponds to the economic question of adequacy of actual and potential substitutes—that it cannot reasonably support a presumption of market power. Treating an intellectual property right as giving rise to such a presumption is all the more consequential an error to the extent that a requirement of market power itself is central to any sound condemnation of tying.

This brief focuses on the policy reasons for this Court to affirm the centrality of a strong requirement of affirmative proof of market power as a threshold condition of establishing tying liability in the first place. *Jefferson Parish*, 466 U.S. at 12-14 (market power required for tying to force buy-

er's purchase of a tied product it does not want or wants to buy elsewhere); *see Eastman Kodak*, 504 U.S. at 464 (same); *Grappone*, 858 F.2d at 794-95 (antitrust concern with tying is limited to sellers with "significant market power"). Given the prevalence and significance of efficiency justifications for tying, the difficulty of identifying circumstances where tying causes antitrust harm, and the uncertainties of the other elements of current tying doctrine, a strict requirement of affirmatively proved market power over the tying product—along with, indeed, a likelihood of such power over the tied product—is an essential screen for tying claims. Without such power, there is no sound basis for treating tying as suspect, and tying law would likely do more harm than good.

A. Conduct Typically Attacked As Tying Is Unilateral In Nature And Thus Subject To The Strong Preconditions For Antitrust Intervention Especially Applicable To Unilateral Conduct

1. This Court has observed that the Sherman Act treats unilateral and concerted action differently. In particular, an especially strong presumption against antitrust intervention applies to unilateral conduct, as distinguished from concerted action that takes the form of promises about how the parties will make future choices about what they buy or sell. *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 767-69 (1984); *see* 3A P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 772d, at 192-93 (2d ed. 2002); *Trinko*, 540 U.S. at 410 n.3 (distinguishing concerted from unilateral refusals to deal). The dichotomy reflects an elementary truth: unilateral action that harms rivals is inherent in competition, and so restricting it through antitrust law carries distinctive risks of harming competition itself. *Copperweld*, 467 U.S. at 767-68 (harm to rivals inherent in competition; unilateral conduct governed by standards that seek to "reduce[] the risk that the antitrust laws will dampen the competitive zeal of a single aggressive entrepreneur").

Conduct commonly attacked as tying falls on the unilateral side of the line.[2] Not only is there no "conscious commitment to a common scheme designed to achieve an unlawful objective," the normal requirement for a conspiracy. *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764 (1984). In addition, conduct attacked as tying ordinarily involves nothing but the defendant's unilateral choice of what to sell, which a plaintiff can frequently characterize as involving two items or services together. Such conduct involves no promise by the buyer to refrain from dealing with other firms or, indeed, any promise regarding future purchases at all.

In this respect, tying, in defining what to sell, is akin to price setting, which defines what to charge. The sale involved in both circumstances can have an effect on the buyer's potential transactions with the defendant's rivals, but

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[2] We put aside cases involving a buyer's promise not to deal with a rival seller, which is only awkwardly described as a "tying" arrangement (rather than "exclusive dealing") in any event. We note, too, that the substantive policy distinction discussed in text is not identical to the distinction between Section 1 and Section 2 of the Sherman Act. On one hand, the distinction between suspect concerted action and the kind of contract that is inherent in the simple purchase of a tying and tied product is important even if the purchase contract suffices to trigger Section 1 of the Sherman Act. On the other hand, agreements are among the actions that have been held to be monopolizing acts under Section 2. *E.g.*, *United States v. Microsoft Corp.*, 253 F.3d 34, 60-65, 67-76 (D.C. Cir. 2001) (en banc).

While the buyer's agreement to purchase the tied product has been treated as satisfying Section 1's requirement of concerted action, *see, e.g.*, *Systemcare, Inc. v. Wang Labs. Corp.*, 117 F.3d 1137, 1145 (10th Cir. 1997) (en banc), Section 1 has been held to require a showing that the challenged agreement "*itself* affected competition in ways that would not have obtained absent the agreement," *Dickson v. Microsoft Corp.*, 309 F.3d 193, 210 (4th Cir. 2002) (emphasis added); *see id.* at 208 (without horizontal agreement among buyers, each defendant's alleged tying arrangement "when considered individually" must be "capable of causing . . . substantial harm to competition").

the effect is no more than that of any sale: it might de facto displace the buyer's need to buy from a rival. Defining what to sell and defining what to charge are inherent in any firm's unilateral conduct in the marketplace. Tying should therefore be subject to the especially strong demand for coherent affirmative proof, and judicial caution, in applying the powerful antitrust remedies to restricting unilateral conduct.

2. At least two related premises support the demand for special justification before antitrust law intervenes to restrict unilateral conduct—premises that squarely apply to tying claims. *First*, antitrust policy is disserved by rules of law that discourage any firm, including a monopolist, from adopting efficient practices and vigorously competing to the detriment of rivals. Consumers suffer from such self-restraint. Not only do they miss the direct benefits (*e.g.*, of lower prices enabled by the efficiencies), but they are harmed indirectly, as actual and potential rivals can afford to be lazy under the monopolist's "umbrella"—rivals are forced to do less, whether through innovative leap-frogging or otherwise, to match or to improve upon the monopolist's offerings if the monopolist is "pulling its competitive punches." *Olympia Equip. Leasing Co. v. W. Union Tel. Co.*, 797 F.2d 370, 375 (7th Cir. 1986) (per Posner, J.).

Second, it is hard to distinguish legitimate rival-harming unilateral conduct from conduct that should be condemned through antitrust law. *See Trinko*, 540 U.S. at 408 (relying on "the difficulty of identifying and remedying anticompetitive conduct by a single firm"); *id.* at 414 ("Under the best of circumstances, applying the requirements of § 2 'can be difficult' . . . . "); *Copperweld*, 467 U.S. at 767-68 ("it is sometimes difficult to distinguish robust competition from conduct with long-run anti-competitive effects"); Evans & Padilla, *Designing Antitrust Rules for Assessing Unilateral Practices: A Neo-Chicago Approach*, 72 U. Chi. L. Rev. 73, 73, 75 (2005) ("the welfare effects of unilateral practices [including tying] are inherently difficult to assess"). Two leading economists explain: "One problem that haunts most antitrust litigation . . . is that vigorous competition may look very similar to acts that *undermine* competition and support monopoly power. The resulting danger is that the courts will prohibit, or the antitrust authorities will prosecute, acts that *appear* to be anticompetitive but that really are the opposite. The difficulty is that effective competition by a firm is always tough on its rivals." W. Baumol & A. Blinder, *Economics: Principles and Policy* 425-26 (8th ed. 2000) (paragraph break omitted); *Concord v. Boston Edison Co.*, 915 F.2d 17, 21 (1st Cir. 1990) (per Breyer, C.J.) ("almost all business activity, desirable and undesirable alike, seeks to advance a firm's fortunes at the expense of its competitors"); *id.* at 23 ("Merely eliminating competitors is not necessarily anticompetitive, for, as we explained earlier, even legitimate business activity that succeeds in helping a firm will likely disadvantage the firm's competitors.").

Antitrust rules that restrict unilateral conduct therefore must guard against multiple dangers. To begin with, they must try to minimize case-specific social costs. Thus, they must seek to avert false positives—antitrust condemnation of conduct that should be allowed—which are "'especially costly, because they chill the very conduct the antitrust laws are designed to protect.'" *Trinko*, 540 U.S. at 414 (quoting *Matsushita Elec. Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574, 594 (1986)); *see id.* ("The cost of false positives counsels against an undue expansion of § 2 liability."). And the applicable antitrust rules must seek to keep the sheer costs of the antitrust litigation as low as possible. Case-specific error and administration costs are reason enough to demand clear screening mechanisms for meritless claims.

Lowering systemic costs is at least as important in framing sound standards for antitrust intervention. A business's decision whether to adopt or not to adopt a legitimate, but rival-

harming, practice will inevitably be influenced by its prediction both of how likely it is that the practice will be erroneously condemned in antitrust litigation (initiated by, *e.g.*, the harmed rival or a customer class action), generating treble damages and attorneys' fees, and of what the costs will be of defending the practice. *See South Austin Coalition Community Council v. SBC Communications Inc.*, 191 F.3d 842, 845 (7th Cir. 1999) ("[a]ntitrust litigation can be very costly"); *Virgin Atlantic Airways Ltd. v. British Airways PLC*, 257 F.3d 256, 263 (2d Cir. 2001) ("Wasteful trials and prolonged litigation that 'may have a chilling effect on procompetitive market forces' should be avoided."). Not only substantively overbroad rules, but rules that are difficult, vague, or otherwise unpredictable in application, and rules that simply require costly litigation, all will deter businesses from engaging in legitimate competition. Easterbrook, *The Limits of Antitrust*, 63 Tex. L. Rev. 1, 14-15 (1984), and encourage use of litigation as a tool to dampen vigorous rivalry.[3] Any articulated basis for antitrust intervention, at least for unilateral conduct, simply cannot be justified without careful consideration of these real-world costs and a consequent effort to define workable threshold requirements

[3] *See* Baumol & Ordover, *Use of Antitrust To Subvert Competition*, 28 J. L. & Econ. 247, 254 (1985) ("[O]bscurity and ambiguity are convenient tools for those enterprises on the prowl for opportunities to hobble competition. As we know, it is not always necessary to win cases in order to blunt a rival's competitive weapons. Harassment by lawsuit or even the threat of harassment can be a marvelous stimulus to timidity on the part of competitors. The potential defendant who cannot judge in advance with any reasonable degree of certainty whether its behavior will afterward be deemed illegal is particularly vulnerable to guerrilla warfare and intimidation into the sort of gentlemanly competitive behavior that is the antithesis of true competition."); *id.* at 264 ("Mere accusation and trial subjects the defendant firm to enormous expenses and even greater ex ante risks of an expensive adverse decision, even if it transpires ex post on the basis of convincing evidence that it is completely innocent.").

that protect against such systemic chilling of investment and vigorous competition.

Serious attention to these considerations is essential to prevent antitrust doctrine from turning the Sherman Act into a weapon for undermining the very policies the Act is supposed to promote. This Court relied on just such considerations in carefully limiting the grounds of antitrust intervention not only in *Trinko*, 540 U.S. at 407-08, but in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 223, 226-27 (1993). Similar considerations were clearly articulated in two First Circuit opinions written by then-Judge Breyer.[4]

Antitrust policy thus requires several questions to be asked for any sound formulation of a ground of condemnation. Based on the difficulty or ease of making the judgments required by a rule, and an empirical sense of the relative frequency of legitimate versus illegitimate uses of the practice at issue, how many false positives will a rule of law directed to a particular practice generate, and how many false negatives? What are the costs of making the crucial distinctions

[4] Judge Breyer explained that, "while technical economic discussion helps to inform the antitrust laws, those laws cannot precisely replicate the economists' (sometimes conflicting) views. For, unlike economics, law is an administrative system the effects of which depend upon the content of rules and precedents only as they are applied by judges and juries in courts and by lawyers advising their clients. Rules that seek to embody every economic complexity and qualification may well, through the vagaries of administration, prove counterproductive, undercutting the very economic ends they seek to serve." *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 234 (1st Cir. 1983). He later elaborated that antitrust rules "must be clear enough for lawyers to explain them to clients," "administratively workable," and "designed with the knowledge that firms ultimately act, not in precise conformity with the literal language of complex rules, but in reaction to what they see as the likely outcome of court proceedings." *Concord v. Boston Edison*, 915 F.2d at 22. *See also* D'Amato, *Legal Uncertainty*, 71 Cal. L. Rev. 1 (1983) (describing costs of legal uncertainty).

required by the rule, and what are the systemic costs for private businesses that have to live with the rule? And, as between courts and the marketplace, which is more likely to correct errors, and after how long, and at what cost (erroneous judicial condemnations have to be corrected by later changes in law, erroneous judicial vindications have to be corrected by market displacement)? *See* Evans & Padilla, at 80-88; Hylton & Salinger, *Tying Law and Policy: A Decision-Theoretic Approach*, 69 Antitrust L.J. 469, 498-502 (2001).

"The costs of false convictions in antitrust decisions involving unilateral practices are likely to be significantly larger than those of false acquittals." Evans & Padilla, at 83. At least in general, the skepticism about antitrust intervention for unilateral conduct may be viewed as a presumption that the marketplace is a better corrective mechanism than the courts (or Congress). Expunging antitrust decisions that unsoundly restrict competitive conduct takes considerable time and effort, whereas allowing a practice that builds or reinforces monopoly power, if that power is exploited, invites entry. *Id.*; *see* Easterbrook, at 15. Our economic system is built on the general judgment that the incentive for profit (by those developing innovations and otherwise seeking entry when markets are monopolized) is a powerful force for undoing monopoly, just as the presumptively protected opportunity to charge monopoly prices "is what attracts 'business acumen' in the first place." *Trinko*, 540 U.S. at 407.

The required analysis, as applied to tying, makes clear the importance of strictly requiring affirmative proof of market power.

B. Tying Is Pervasive, Including In Competitive Markets, And Commonly Carries Benefits, Though The Benefits Are Hard To Prove

The early rule against tying reflected the belief that "tying arrangements serve 'hardly any purpose beyond the suppression of competition.'" *Jefferson Parish*, 466 U.S. at 34 (O'Connor, J., concurring in the judgment) (quoting *Standard Oil Co. v. United States*, 337 U.S. 293, 305-06 (1949)). *Jefferson Parish* recognized that the early belief was mistaken. Referring to a seller's "refusal to sell two products separately," the Court observed that "[b]uyers often find package sales attractive" and "a seller's decision to offer such packages can merely be an attempt to compete effectively—conduct that is entirely consistent with the Sherman Act." 466 U.S. at 12.

Continued study has deepened the understanding that tying is frequently beneficial. To begin with, it is now widely recognized that "tying is pervasive," even where it is taken as a given that there are separate products. Evans & Padilla, at 89. "Cars only come with air conditioners, mobile phones with ring tones, newspapers with arts sections, law school curricula with courses on torts, computer operating systems with internet-communication protocols, and cameras with built-in flashes." *Id.* at 90. *See also* Evans & Salinger, *Why Do Firms Bundle and Tie? Evidence from Competitive Markets and Implications for Tying Law*, 22 Yale J. Reg. 37, 40-41 (2005); Hylton & Salinger, at 486 ("A moment's reflection reveals that tying is utterly ubiquitous."); *id.* at 498 & n.113.

More particularly, "tying is common in competitive markets." Evans & Salinger, at 40, 83. That fact establishes that tying widely carries efficiency benefits. Broad and persistent adoption of a practice in a competitive market powerfully indicates efficiency because competition from rivals otherwise would force abandonment of the practice. *See* Evans & Padilla, at 81 ("Consider a practice in which firms in both competitive and uncompetitive markets engage. We would expect that the practice cuts costs or enhances value—after all, competitive firms cannot survive indefinitely if they do not use the most efficient methods of producing, designing, and distributing products."); Hylton & Salinger, at 497-98

("the prevalence of tying in competitive markets indicates that it often provides the economic benefits of providing convenience and lowering costs"). "There is no economic reason to believe that these efficiencies become less important as firms acquire market power." Evans & Padilla, at 81; *id.* at 91 (the "sources of efficiency remain, regardless of the degree of market power of the firm engaging in the practice"); Evans & Salinger, at 42. And firms with market power have an incentive to pass on at least some of the benefits to their customers. Hylton & Salinger, at 504. Accordingly, "[i]f the practice is one employed widely in industries that resemble the monopolist's but are competitive, there should be a presumption that the monopolist is entitled to use it as well. For its widespread use implies that it has significant economizing properties, which implies in turn that to forbid the monopolist to use it will drive up his costs and so his optimum monopoly price." R. Posner, at 253; *see* Epstein, *Monopoly Dominance or Level Playing Field? The New Antitrust Paradox*, 72 U. Chi. L. Rev. 49, 60 (2005).

Based on the prevalence of tying in competitive markets, "[t]oday it seems quite clear that most tie-ins benefit competition, even when the defendant has tying product power." 9 P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 1720a, at 220 (2d ed. 2004) (footnote omitted). The benefits are various. Offering two products only together can provide customer convenience and can lower marginal costs of production, packaging costs, delivery and other transaction costs, and costs of dealing with product complexity. *See* Evans & Salinger, at 43, 52; Evans & Padilla, at 90-91; Hylton & Salinger, at 485-86, 504.[5] Other benefits include efficient quality control

[5] As one simple illustration of cost savings, consider a firm selling widgets (the tying product) and gadgets (the tied product). "Suppose for example that 80% of the purchasers of widgets also want gadgets, that gadgets cost $1 to produce, and that the incremental cost of packaging gadgets separately from widgets is $0.30. In this example, it is cheaper to provide a gadget for those who do not want it (a cost of $1 per customer for 20% of the customers) than it is to package the goods separately ($0.30 per customer for 80% of the customers)." Hylton & Salinger, at 503.

and economies of scale easing entry into a tied product market. 9 *Antitrust Law* ¶ 1703g, at 44-46, ¶¶ 1711-1718h, at 100-214; 10 P. Areeda, H. Hovenkamp, & E. Elhauge, *Antitrust Law* ¶¶ 1761-1764e, at 357-98 (2d ed. 2004); *see* Meese, *Tying Meets the New Institutional Economics: Farewell to the Chimera of Forcing*, 146 U. Pa. L. Rev. 1, 10, 59-66, 74-84 (1997).

While the ubiquity of tying in competitive markets confirms the reality of its benefits, the kinds of benefits conferred by tying are commonly difficult to prove. "It is not surprising that businesses have difficulty documenting and sometimes even articulating efficiencies. In reality, businesses operate instinctively and often cannot show that their prices are profit maximizing or that they are minimizing costs—even though we assume successful businesses gravitate toward best practices. The efficiency gains from practices such as tying and distribution agreements are often subtle and not readily reduced to accounting numbers." Evans & Padilla, at 82; *see* Evans & Salinger, at 83 (Tying "results in lower costs for producers—which get passed on to consumers—or greater convenience, which benefits consumers directly. But these cost savings for producers and consumers are not necessarily easy to document."); *id.* at 85-86 ("even in competitive industries where we are confident that efficiencies are the only plausible explanation for the practice, solid empirical evidence is not easy to produce"). With tying as with many other competitive practices, "[e]fficiencies are hard to measure, and the benefit of the doubt should go to defendants, not to plaintiffs; otherwise, the continued generation of the large efficiency benefits responsible for raising our standard of living will be jeopardized." Carlton, *A General Analysis of Exclusionary Conduct and Refusals to Deal—Why* Aspen *and* Kodak *Are Misguided*, 68 Antitrust L.J. 659, 675 (2001).

For these reasons, a tying law rule that condemns tying without inquiry into efficiencies would produce erroneous condemnations (and deter still further beneficial ties). And so too would a standard that allows such inquiry but places a substantial burden on defendants to prove such efficiencies. Evans & Salinger, at 86.

C. Antitrust Harm From Tying, Which Requires Market Power, Is Difficult To Identify

The Court has already made clear that market power is one necessary condition for condemning a tie. *Jefferson Parish*, 466 U.S. at 14-16; *see Eastman Kodak*, 504 U.S. at 464. A tying violation also requires separate products, forcing of customers seeking the tying product also to take the tied product, and certain effects on the tied-product market. *See, e.g., id.* at 461-62; 9 *Antitrust Law* ¶ 1702, at 27-30. Those conditions alone, however, are insufficient to draw a sound inference of antitrust harm, both because of the existence of efficiencies and for other reasons. *See, e.g.*, Evans & Padilla, at 82 ("The principal implication of several decades of economic investigation on the competitive effects of unilateral practices, such as exclusive dealing and tying, is that there should be *no* presumption . . . that these practices are anticompetitive, even when undertaken by firms with monopoly power.") (footnote omitted); Evans & Salinger, at 85 ("As a matter of theoretical and empirical economics, the modified per se test is not capable of identifying anticompetitive tying except by happenstance. The single-product test, which examines whether the tying and tied good are part of a 'single product,' is not a reliable proxy for examining whether there are efficiencies or not."); 9 *Antitrust Law* ¶ 1730, at 351-59.

In *Grappone*, then-Judge Breyer explained that "tying's anticompetitive mechanism is not obvious." 858 F.2d at 794. In a typical situation, a firm with monopoly power in the tying product can exploit its power through the price it

charges for that product and gains no additional monopoly profits by tying. *Id.* at 795. As Judge-Breyer explained:

> If the Seller does not have market power in respect to Product A, it cannot force buyers to take a more expensive or less desirable Product B, for if the Seller tries to do so, buyers will simply turn elsewhere for Product A. If the Seller does have, and has been fully exercising, market power, it also cannot force buyers to take a more expensive or less desirable Product B, *unless* it provides buyers *equivalent* compensation by lowering the price of Product A (or maintaining Product A's price at a level lower than the Seller has the *power* to charge), for otherwise buyers, who were already paying as much as the Seller could charge them (with its degree of market power) would also likely switch to other sellers or discontinue use of Product A.

Id. at 795. In such circumstances, efficiency is the presumptive explanation for tying.

Any market harm requires a more complex set of conditions, keyed to genuinely constricting competition in the tied product. *Id.* at 795-96. In particular, as Judge Breyer explained, *Jefferson Parish* itself recognized that the mechanism of market harm from tying applies only if the seller "first hurts firms seeking to sell the *tied* product. Only if the tie significantly reduces the opportunities to sell Product B" can there be market harm. 858 F.2d at 796, citing *Jefferson Parish*, 466 U.S. at 14. What is required is that the tie "permit[] the Seller to extend its market power from one level to two," *i.e.*, threaten to gain market power in the tied product market, so that buyers are forced to rely on the seller for their tied product as well as the tying product, and a new entrant would be forced to enter both lines of business in order successfully to reach potential buyers. 858 F.2d at 795-96. As a logical matter, then, the effect on the tied product market that is necessary (but not sufficient) for any sound inference of antitrust harm is one of at least a dangerous probability of

market power in that market. *See Carl Sandburg Village Condominium Assn. No. 1 v. First Condominium Dev. Co.*, 758 F.2d 203, 210 (7th Cir. 1985); 9 *Antitrust Law* ¶ 1722d, at 260.

Newer economic models (referred to as "post-Chicago" literature) have described, theoretically, some circumstances where a monopolist might gain additional profits by tying. That is not by its terms a sufficient basis for condemnation. More specifically, the limitations of this literature are as important as the "possibility theorems" it presents. Evans & Padilla, at 78-79, discussing, in particular, Whinston, *Tying, Foreclosure, and Exclusion*, 80 Amer. Econ. Rev. 837 (1990), and Carlton & Waldman, *The Strategic Use of Tying to Preserve and Create Market Power in Evolving Industries*, 33 RAND J. Econ. 194 (2002); *see* Hylton & Salinger, at 488-95.

First, the models *add* to the requirement of a "monopoly" in the tying product (Evans & Padilla, at 78) further preconditions about likely constriction of the tied product market (*e.g.*, scale economies or other entry barriers in the tied-product market). *Second*, the most the models do is show that a monopolist sometimes might earn more profits by tying; they say nothing about whether those circumstances are actually likely to arise, let alone how to identify them reliably. Hylton & Salinger, at 497 ("the models cannot tell us even that anticompetitive tying is more than a remote possibility"). *Third*, as important, showing the ability to gain more profits (within the circumstances theoretically identified) is *not* the same as showing market harm, for these models expressly assume away efficiencies; *i.e.*, they effectively deal with only half the required inquiry even for a case-specific analysis. Evans & Padilla, at 79; Evans & Salinger, at 51; Hylton & Salinger, at 506. Thus, even in the circumstances hypothesized, they do not find the absence of net consumer benefit based on the tying arrangement's generating more profits (deservedly) because it enhances consumer value. *Fourth*,

the models do not (even purport to) proceed to the next essential stage of examining the systemic positives and negatives of an antitrust rule allowing litigation to try to sift the chaff from the wheat. *Fifth*, in fact, the narrow assumptions in the new models are very sensitive (minor alteration changes the conclusion) and are difficult to identify with any reliability. *See* Evans & Padilla, at 74 ("since the models are highly sensitive to specific assumptions and parameter values, they do not provide much practical guidance"), 79-80, 90 n.67 & 91 (models' limits stressed by their creators); *id.* at 98 ("the post-Chicago literature . . . has yet to demonstrate a capacity to produce . . . useful descriptions of the circumstances determining whether a practice is procompetitive or anticompetitive"); Evans & Salinger, at 41 ("Foreclosure theories show that tying could be anticompetitive under special conditions that are difficult and perhaps impossible to verify in practice."), 51-52[6]; Hylton & Salinger, at 488-95, 497, 506-07.

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[6] "The models demonstrate the theoretical possibility of tying to foreclose entry. They thereby provide a necessary correction to the Chicago view (among some adherents) that profitable foreclosure is never possible. The new models rest, however, on very restrictive assumptions. One is that bundling generates no efficiencies. Without allowing for possible efficiencies, the models cannot weigh the offsetting welfare effects of efficiency and foreclosure. Moreover, even if one were to incorporate efficiencies into the models, the remaining assumptions are so stylized that it is hard to know when they apply—if ever. As it currently stands, the literature represents a significant scholarly contribution which, with further work, might yield useful policy insights. The existing literature by itself, though, does not give the antitrust authorities or the courts much practical guidance on how to determine whether a particular tie harms consumer welfare." Evans & Salinger, at 51 (footnotes omitted). Carlton and Waldman, notably, have stated cautions about the use of their model in imposing antitrust liability. Carlton & Waldman, *How Economics Can Improve Antitrust Doctrine Towards Tie-In Sales*, 1 Competition Policy Int'l 27, 29, 40 (2005).

In short, antitrust harm from tying remains dauntingly difficult to identify reliably even with the firm requirement of monopoly power over the tying product. Certainly there is no basis for permitting condemnation of any tie that does not begin with such power. And in fact the literature powerfully supports the conclusion that the required effect in the tied-product market is one of probable market power. A strong screening mechanism is needed to reduce the risk of condemnation, or deterrence, of ties that are beneficial rather than harmful.

D. Litigation Under Existing Tying Doctrine Carries Substantial Costs And Uncertainties

The need for a market power screen for tying claims is reinforced by the problematic character of the other elements of current tying doctrine. Notably, "[i]t has often proven difficult to decide whether a transaction really involves two different products and whether they have been 'tied' together, because the tying concept has become widely elastic." 9 *Antitrust Law* ¶ 1720a, at 220 (footnote omitted). The result is a high risk of error for courts applying current law and great uncertainty for businesses contemplating the possibility of costly litigation.

1. One threshold requirement for a tying claim is to demonstrate the existence of separate products. *Jefferson Parish*, 466 U.S. at 18-22; *see Eastman Kodak*, 504 U.S. at 462. But "[w]hen a bundle constitutes separate products rather than a single product is often unclear. This problem has become more noticeable as plaintiffs have become ever more creative in characterizing transactions as involving separate products . . . . " 10 *Antitrust Law* Ch. 17D-1, at 151. And "[t]he problem is pervasive because just about any product could be described as a tie of its components." *Id.* Yet the legal approaches to answering the doctrinal question—whether there is "sufficient consumer demand so that it is efficient for a firm to provide" the two allegedly separate products separately (*Eastman Kodak*, 504 U.S. at 462; *Jefferson Parish*, 466 U.S. at 21-22)—are complex, uncertain, and difficult to apply. The leading treatise devotes more than 100 pages just to this element of tying law. 10 *Antitrust Law* ¶¶ 1741-1751f, at 151-260. *Compare Jefferson Parish*, 466 U.S. at 24 (anesthesia and surgery "two distinguishable services") *with id.* at 43 (O'Connor, J., concurring in the judgment) ("no sound economic reason for treating surgery and anesthesia as separate services").

Markets characterized by innovation—as when new technologies change the nature of products or services—present special complications. Notably, the *Jefferson Parish* approach to testing whether a defendant's practices involve separate products is a "poor fit" for new offerings to the extent that it looks to *others*' practice, which may, almost by definition, provide an inapt comparison. *United States v. Microsoft Corp.*, 253 F.3d 34, 85 (D.C. Cir. 2001) (en banc).[7] Moreover, when an industry is undergoing technological change, there is at least some reason to think that the risk of harm from a less interventionist approach to tying is generally

[7] *Id.* at 89 ("The per se rule's direct consumer demand and indirect industry custom inquiries are, as a general matter, backward-looking and therefore systematically poor proxies for overall efficiency in the presence of new and innovative integration. *See* 10 AREEDA ET AL., ANTITRUST LAW ¶ 1746, at 224-29; Amicus Brief of Lawrence Lessig at 24-25, and sources cited therein (brief submitted regarding Conclusions of Law). The direct consumer demand test focuses on historic consumer behavior, likely before integration, and the indirect industry custom test looks at firms that, unlike the defendant, may not have integrated the tying and tied goods. Both tests compare incomparables—the defendant's decision to bundle in the presence of integration, on the one hand, and consumer and competitor calculations in its absence, on the other. If integration has efficiency benefits, these may be ignored by the *Jefferson Parish* proxies. Because one cannot be sure beneficial integration will be protected by the other elements of the per se rule, simple application of that rule's separate-products test may make consumers worse off.").

lower. The self-correcting mechanism of the market (reacting to judicial false negatives) would seem generally to work especially well when technological change allows rivals to jump beyond a current monopolist's technology, whether by full-scale replacement or by innovations that combine partial substitution with other benefits the monopolist is not offering. *See* Hylton & Salinger, at 513.

Further, in technologically changing markets, product definition itself may be especially fluid, and therefore unreliable. Tying may even by key to creation of new product markets—as when, for example, cable television service changed from retransmitting a few broadcast television signals to offering many-channel packages, thereby creating a market for multi-channel video programming distribution (MVPD) services. *See* FCC, *Report on the Packaging and Sale of Video Programming Services to the Public* 62 (Nov. 18, 2004) ("The bundling of channels into tiers of services is, generally, an economically efficient way of providing MPVD subscribers with video programming."). Condemning a tie may perpetuate a separate market for each constituent and obstruct the evolution of a new composite product market.

2. The "forcing" requirement of tying law, which cannot reliably suggest whether a challenged tying arrangement is efficient or inefficient, can also be difficult and uncertain. Some cases involve a defendant's unambiguous requirement to buy two products together. But plaintiffs sometimes seek to prove forcing by showing that the pricing terms are such that customers can hardly make a rational economic choice but to take the tied product along with the tying product—because the package price and the tying-product price are sufficiently close. *See* 10 *Antitrust Law* ¶ 1758, at 323-36; Hylton & Salinger, at 510. The resulting inquiry can easily demand tasks for which this Court has noted the courts are not well suited. *Trinko*, 540 U.S. at 408 ("identifying the proper price, quantity, and other terms of dealing [is] a role

for which [the courts] are ill-suited"); *see Concord v. Boston Edison Co.*, 915 F.2d at 25. The difficulties can prompt courts to turn to substitutes for the inquiry that are even more unpredictable and subjective, and ungrounded in any economically coherent and workable rule that preserves for customers the benefits of package pricing. *Cf. LePage's Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003) (en banc), *cert. denied*, 124 S. Ct. 2932 (2004) (Section 2 package pricing); *see* Crane, *Multiproduct Discounting: A Myth of Nonprice Predation*, 72 U. Chi. L. Rev. 27 (2005) (criticizing *LePage's* decision); Rubinfeld, *3M's Bundled Rebates: An Economic Perspective*, 72 U. Chi. L. Rev. 243 (2005) (same).

3. The costs of erroneous legal condemnation under tying doctrine are particularly great if efficiencies are ruled out of the inquiry, because a finding of antitrust harm cannot soundly be made if the elements of tying exclude such inquiry. So recognizing, courts have allowed efficiency, or justification, inquiries in a variety of tying cases. *See Microsoft*, 253 F.3d at 94-95; 10 *Antitrust Law* ¶ 1760c, at 347 ("The lower courts have consistently considered justifications in principle, approving ties for all the reasons that the Supreme Court has suggested, plus additional ones.") (footnote omitted). On the other hand, once the inquiry is allowed (in order to avoid a rule that is in its very terms overintrusive), the expense and difficulties of the litigation increase, and so do the uncertainties. As already noted, it is hard to assess the relevant efficiencies—even when the prevalence of the practice in competitive markets establishes that they are likely to be significant.

E. A Strict Threshold Requirement Of Affirmatively Proved Market Power Is Essential For Any Tying Claim

For all the foregoing reasons, tying law carries high risks of case-specific error and broad potential to inflict systemic harm from deterring the adoption of efficient practices simply

because of the costs and risks of litigation. The problem would not be solved by simply announcing a general rule of reason approach to evaluating the harms and benefits of a challenged tying arrangement, without significant *threshold* requirements to eliminate the broad classes of tying arrangements that, as a matter of precedent and economic analysis, cannot be found, reliably and without overriding systemic risks, to cause consumer harm.[8] The need for meaningful screens is reinforced by the policy judgment that the costs of rules inviting undue intrusion on unilateral conduct such as tying are likely to be greater than the costs of rules that may generate some false negatives.

The most obvious minimum requirement for a sound tying standard is affirmative proof of market power over the tying product—along with a requirement that market power over the tied product be proven dangerously probable. There is no substantial possibility of harm (or forcing) without such market power. *Grappone*, 858 F.2d at 795-96; *see* Hylton & Salinger, at 503; 10 *Antitrust Law* ¶ 1734b3, at 39 ("no tying arrangement can harm competition in the tied market absent 'power' in the tying market"). Where market power over the tying product is lacking, indeed where a high degree of market power is lacking, buyers can turn to others for the tying product, and that ability is a better constraint on any damaging tying arrangements than any rule of law. R. Posner, at 265 ("[H]ow can a firm with only 30 percent of a market exclude competitors by tying two products together? A firm that wants to produce only one of these products will have no

[8] *See* Evans & Padilla, at 75 n.8 (Judge Easterbrook in 1984 "emphasized the importance of presumption in structuring antitrust inquiries" and "observed that the full rule of reason approach is often impractical"; all the more so today, for with "the benefit of over twenty years of game-theoretic industrial organization models . . . . [we are] skeptical about the ability of economics to provide the necessary guidance for a full-blown rule of reason inquiry").

difficulty finding customers."). And without likely market power over the tied product, the tying arrangement cannot reliably be found to enhance the seller's ability to charge supracompetitive prices in the short or long run. *Cf. Trinko*, 540 U.S. at 415 n.4 (rejecting "leveraging" without dangerous probability of market power in the second market).

A strict requirement of affirmative proof of market power can matter considerably in practice. The burden of proof and an explanation by this Court that the requirement must be enforced rigorously can diminish the adverse market effects of a looser tying standard. Such formulations can make a difference in screening out, even in the decision whether to launch litigation, claims for which a reliable case of harmful tying can never be made. And they can make a large difference in reducing the costs and risks of litigation.

In particular, summary judgment must be granted to the defendant if the plaintiff cannot meet its burden of proof on an essential element. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 254-57 (1986); *Celotex Corp. v. Catrett*, 477 U.S. 317, 322-23 (1986). The burden of proof is most important – is intended to be dispositive—precisely on matters that resist reliable resolution, because adequate information is unavailable or for other reasons. *See Cruzan v. Director, Missouri Dep't of Health*, 497 U.S. 261, 282-83 (1990). It is therefore an important element of antitrust cases. And, with a serious market power standard that can be applied at the summary judgment stage, in many cases the costs of litigation can be dramatically reduced by a district court's narrowing discovery to focus on market power as a prelude to a summary judgment motion.

In short, general antitrust analysis makes clear that the requirement of affirmatively proven market power is so critical to any sound tying-law standard that it must be carefully preserved. The Court should reinforce the requirement in this case. And it should reject the watering down of this impor-

tant requirement effected by the unsound presumption of market power based on a patent or other intellectual property right.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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